NOTES

THE ALDRICH BILL

The measure proposed in the Senate to remedy our monetary and financial ills furnishes another example of the deadening effect of politics, and of a lack of expert knowledge in regard to banking, upon Congress. Nothing could better show the utter misunderstanding of the events we have just passed through than the scheme proposed by the leaders of the Senate. Of course, it will be urged that nothing really sane could be passed; but, to this it should be replied that the proposal of a really sound measure would have educated the public, and in the end would have helped on the possibility of a right solution.

In the first place, the authors of the bill quite fail to comprehend that, in the recent crisis, the inability of banks to lend to needy borrowers was the central difficulty which brought on failures, and cessation of business. If loans could have been had, many a concern would have been able to meet its obligations and continue its productive operations. What limited the power of the banks to lend? Primarily, the limited capital already at their disposal, which had been stretched to its utmost capacity; and directly, the ratio of lawful reserves to demand liabilities in the form of deposits. Since only about 5 per cent. of a bank's receipts in New York are in currency, the deposits are in the main the result of loans. To loan, is to increase the proportion of deposits to reserve. Then, if a panic seizes the public, and even the banks of the interior which deposit in central cities, the lawful reserves are drawn down; and the banks cannot lend to needy borrowers. How, then, can it help the banks in such a crisis to be permitted to issue their own notes? This can help only in so far as putting out their own notes, in a case of a run on the bank, will save their lawful reserves. It is not so much a scarcity of money, when hoarding is going on, as it is directly the amount of reserves and their protection, which is of primary importance. Consequently, one would suppose the Aldrich Bill would have provided notes—as when the Bank Act is suspended in England—which could go into bank reserves, and thus increase the ability of the bank to lend. No such thing is done. On the contrary, the banks are allowed only to increase their

own note liability; and more than this, only at a charge of 6 per cent., increased by usual costs for bonds, etc., to 7 or 8 per cent.

Now, wherein does this provision assist the banks in the least to hold up the business world by loans? In the crisis, they are already estopped from lending because reserves have gone down; and, to a merchant begging for loans to save him from failure, they say: we can give you a loan, and credit you with a deposit of that amount—provided the clearing-house committee will cover your checks as they come in with clearing-house certificates based on our commercial assets—and the checks will pay your obligations at any bank in the city; or, under the Aldrich Bill, if then a law, we could give you a loan, and hand you our bank notes for it—provided you wait until we take out 133 per cent. of the amount of your loan from our lawful reserves, send out and buy some specified municipal, county, or state securities, or railway bonds, send them to the subtreasury, telegraph for authority to issue notes, get them printed in Washington, have them sent back and signed, and then charge you about 7 or 8 per cent. for their cost, independently of the rate of interest for the loan. What under heavens could induce the borrower, or the bank, to choose the latter method? If the bank dare take away any of its precious reserves, then, instead of buying securities on which only 75 per cent. of their value in notes can be issued, why not keep the reserves, and make loans to four times the amount proposed to be used in buying bonds? If $100 invested in bonds will allow an issue of only $75 in notes to cover a loan, then $100 left in the reserve would cover loans to the amount of $400. It is evident, at once, that the Aldrich scheme would only cripple the bank in time of stress, and oblige the borrower to pay enormously for his salvation.

Moreover, the plan seems to be based on the stupidity of supposing that a borrower in need cannot pay his debts by a certified check, but only by bank notes. If a bank never issued a note under the Aldrich Bill, it could help business men to at least five times as much in loans by keeping its reserves, lending, creating the usual deposit account, and giving the borrower the right to draw on demand on that account. To issue more bank notes would not increase its reserves; and a bank's ability to lend is in no way touched by the right to increase—not its reserves—but its liabilities. The Aldrich Bill is another of the curiosities of our currency legislation.

There is the possibility of giving a loan by granting to the borrower a claim on the bank, either in the form of a deposit account, on which he can draw checks, or in the form of the bank's own notes. Both are a demand liability; and the discount, or profit to the bank, is the same, whichever form is used. Therefore, to tax one form 7 or 8 per cent. will work merely to cause the other form to be used; or, in other words, the notes of the Aldrich Bill, by its own provisions, are made practically non-usable. Hence, in a crisis, the bill would be no help whatever; and banks would be forced, just as now, to resort to clearing-house certificates. Fortunately those certificates are still left as a means to be resorted to in the next crisis.

In a condition of great stress, moreover, how are the three gentlemen in Washington to know whether it is wise to allow a Chicago bank to make a loan, and give the borrower its own notes? First of all, they ought to pass upon the collateral offered, or upon the condition of the borrower's own business—as is done by a clearing-house committee, with great effectiveness, when certificates are issued. Such a suggestion implies a quality of naïveté in Congress which would grace a child of six, but disgrace a man of sixty. Either the government should supervise all loans, or else it should keep out of the banking business altogether.

Again, if the right to issue these emergency notes is confined to banks already having outstanding notes, secured by United States bonds, to an amount of not less than 50 per cent. of their capital stock, it should be noted that large banks in New York and elsewhere—which notoriously have not issued any notes to speak of—would, for very definite reasons, other than those mentioned above, be inhibited from resorting to any issues under the Aldrich Bill. In short, a more clumsily devised scheme—or one devised, perhaps, how not to do anything—could hardly be conceived of.

In favor of the bill, it should in fairness be said that it wipes out the restriction on the retirement of bank notes fixed by the act of March 4, 1907, at $9,000,000 per month. That, at least, is a step ahead. Such elasticity as comes from the ability to contract notes, when no longer needed, is obtained by the measure; but that which comes from expansion is wholly absent. Any issues of notes based on bonds are less profitable to a bank at the time when most needed by the public, and more profitable at a time when least needed. As to this admitted principle the Senate leaders are seemingly indifferent.

Also, so far as the putting-out of bank notes would meet a run for cash, the bill is to be commended; but the process of providing a currency based on securities practically removes this advantage from consideration, because the run would be over, and the bank closed, before these emergency notes could be obtained.

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RELATION OF PACKERS' CREDIT TO PANIC AND PRICES

The unprecedented decline in the price of hogs, a drop of $2.70 per hundred in six weeks, is one of the incidental results of the recent panic. This phase has received slight attention in the public press or the financial journals. The live-stock journals discuss and explain the situation occasionally but the daily newspapers do no more than chronicle the facts in their market reports. The front pages and editorial columns are filled with comments on the stock market and banking situation as it changes from day to day. A few people, mostly stock gamblers and speculators, are vitally interested in the ups and downs of the stock exchange, but their number is insignificant compared with the number of producers who have hogs, cattle, and sheep to sell. The sums involved in the stock exchange, however, make the two millions of dollars daily paid out to farmers for live stock at the packing centers look insignificant. Nevertheless, it is a very serious matter for the individual farmer or hog shipper to find hogs fifty cents or a dollar a hundred lower when he gets them to market than they were two or three days before when he bought or loaded them. A decline of 20 or 30 per cent. may as easily ruin the hog dealer as a like decline in stocks may ruin the Wall Street dealer.

In the hog market the decline in the average price of hogs between November 17 and November 25 was $1.17 per hundred, from $5.13 to $3.96, or over 22 per cent. Between October 11 and November 25 the decline was $2.70 per hundred-weight, or more than 33 per cent. Indeed, between the extreme high point in October and the low point in November the difference was about 40 per cent. From the extreme low point of $3.96 the price recovered $1.00 in four market days. This was clearly due to the competition of local butchers and purchases for the eastern markets. The